AT&T Comcast will be on a stronger footing in dealing with these substantial business risks because of the complementary assets and expertise of Comcast and AT&T Broadband and the scale economies created by the merged entity. As described in section IV.A, Comcast's financial and management strengths will provide the merged company with a strong balance sheet, a healthy cash flow, and an ability to raise capital, all of which AT&T Comcast will need to deploy telephony services on a broader scale. And, as described below, AT&T Broadband brings to the merged entity extensive experience and expertise in the design, roll-out, provisioning, operations, and marketing of cable telephony in a customer-friendly manner. This expertise is highly scaleable and can be applied to Comcast's cable systems, which currently provide cable-delivered telephone services on only a small scale.

As a result, AT&T Comcast will be better able to expand the availability of telephony over the Comcast systems more quickly, at less expense, and in a more customer-friendly manner. The Applicants estimate that, within five years, leveraging AT&T Broadband's operational and technical expertise in cable telephony should generate synergies of $600-800 million in EBITDA annually.[68] In light of these synergies, Comcast President (and AT&T Comcast CEO) Brian L. Roberts has announced that the merged company intends to begin to deploy telephone service in the Philadelphia and Detroit markets currently served by Comcast after closing, bringing facilities-based local telephone choice to about one million additional homes.[69]

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68 *See* Pick Declaration ¶ 12.

69 As the Pick Declaration indicates, Comcast's experience with cable telephony to date has been relatively limited. Although Comcast has acquired a few existing cable telephony networks through prior acquisitions, these networks are relatively small, and Comcast has not yet developed any new cable telephony networks on its own initiative,

2. Leveraging AT&T Broadband's Substantial Expertise And Experience

AT&T Broadband's cable telephony expertise will enhance the ability of Comcast to offer cable telephony services in two important respects.

Technical and Operational Expertise. Comcast will acquire AT&T Broadband's technical and operational expertise in launching and providing cable telephony. AT&T Broadband has in place the infrastructure and personnel to support the deployment of cable telephony in Comcast service areas. For example, AT&T Broadband has in place centralized systems to support the design, installation, maintenance, and operation of the complex, two-way hybrid fiber-coaxial systems that support digital voice and data applications and that interconnect with both copper twisted-pair and fiber optic technologies used by incumbent LECs.

The AT&T Broadband National Operations team provides support on a wide range of planning, engineering, technical, and operational issues that are faced when deploying complex cable telephony service. The Technical Operations Organization within AT&T Broadband has already developed operational performance metrics to ensure quality cable telephony services, effective training of technicians and field fulfillment personnel, and cost-effective investigation and resolution of field performance issues. That unit also provides subject matter experts for corporate and marketing initiatives. These existing processes and systems, developed at significant cost by AT&T Broadband, can be applied to Comcast's cable systems.

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nor has Comcast developed the experience or infrastructure to expand cable telephony on its own. Pick Declaration ¶ 10. As a result of Comcast's discussions with AT&T Broadband, however, and based on AT&T Broadband's telephony expertise and the resources that will be available due to the merger, Comcast is currently planning to roll-out cable telephony in certain markets after closing. *Id.* ¶ 12.

Cable telephony providers must, of course, be interconnected to, and coordinate with, incumbent LECs (and other competitive LECs) and must interact effectively with a variety of third parties, to ensure not only that calls are completed successfully and billed correctly, but also that all of the necessary number portability, E911, and other databases are correctly populated. This "intimate knowledge of local telephone operations" is vital to the ability to provide quality phone service and cannot be "quickly duplicated by smaller market participants, such as cable operators and [competitive access providers]."[70] AT&T Broadband's National Service Assurance Center supports the provisioning of customer telephone lines, including switch and headend equipment, third party provisioning, local number portability, and E911. Cable telephony providers must also establish interfaces with other LECs for the purpose of rating, recording, and billing traffic for purposes of reciprocal compensation. Again, upon closing, the same organization at AT&T Broadband that now acts as the point of interface for these issues will be available to support cable telephony operations over the Comcast systems. Comcast will also be able to gain the advantage of certain interconnection agreements that AT&T Broadband has with the incumbent LECs serving Comcast's territories.[71]

Back Office Systems. Comcast will gain access to AT&T Broadband's existing back office systems that support cable telephony. These systems allow AT&T

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[70] *See Applications of NYNEX Corporation Transferor, and Bell Atlantic Corporation Transferee, For Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries*, 12 FCC Rcd 19985, ¶ 107 (1997) ("*Bell Atlantic-NYNEX Merger Order*").

[71] AT&T Comcast "will benefit from AT&T's bargaining leverage [and] expertise in negotiating interconnection with ILECs" and "thus [the merger] is likely to enable [AT&T Comcast] to interconnect with ILECs' networks on better terms . . ." *AT&T-MediaOne Merger Order* ¶ 165. AT&T Broadband also has established customer care systems (including an online customer care platform) that can be leveraged to handle billing and network inquiries of Comcast customers.

Broadband efficiently to take customer orders, to serve as the point of contact for customer care inquiries, to collect and organize the data necessary to bill customers, and to market cable telephony offerings. As the Commission has recognized, having in place these "nuts and bolts" back office capabilities and employees is "essential" to offering local telephone service in competition with incumbent LECs.[72] Not only are AT&T Broadband's back office systems highly robust and efficient, but they employ technologies and processes that will allow AT&T Comcast to use them to support offerings in Comcast territories without incurring substantial additional cost.

The combination with AT&T Broadband will also enhance Comcast's telephone billing capabilities. AT&T Broadband has in place specialized "mechanized" billing software processes, developed over several years, that are sufficiently flexible to handle a service area's unique billing parameters and sufficiently robust to handle substantial increases in volume. These back office billing systems can be used to support telephone entry in Comcast territories at a mass market level.

AT&T Broadband's substantial marketing expertise will help Comcast in the challenge of competing for customers against formidable incumbents in Comcast's service areas. AT&T Broadband has already conducted primary market research on topics such as pricing and offer design – benchmarked against the competition – to assist AT&T in developing successful product offers, programs, and marketing campaigns. And AT&T Broadband has learned a tremendous amount about customer preferences

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[72] *See Applications of Ameritech Corp., Transferor, and SBC Communications Inc., Transferee, For Consent to Transfer Control of Corporations Holding Commission Licenses*, 14 FCC Rcd 14712, ¶ 84 (1999) ("*Ameritech-SBC Merger Order*").

(including the types of marketing that customers like and dislike) as a result of its market experience over the past several years.

Summary. The complementary telephony assets and experience of AT&T Broadband and Comcast will put the merged entity on a stronger footing and help accelerate the pace and effectiveness of local telephone competition in Comcast's service areas. Moreover, the operational, back office, and customer care experience AT&T Broadband has gained from its circuit-switched telephony operations should be applicable to an IP telephony environment.[73] As noted in section II.B.1, Comcast has taken a leadership role in developing cable-delivered IP telephony, and AT&T Broadband has explored this technology as well. IP telephony may result in significantly lower roll-out costs and increased flexibility and may also provide a common infrastructure that supports multiple advanced services. The Applicants are committed to the continued development of IP telephony.

C. The Merger Will Increase The Supply Of Local And Regional Programming.

The combination of AT&T Broadband and Comcast will also benefit consumers by stimulating the production and delivery of local and regional programming. Comcast's established expertise in producing local and regional programming will enhance the ability of the merged entity to offer AT&T Broadband customers the kinds of community-oriented coverage that Comcast already provides today to many of its customers. This includes news, public affairs, coverage of civic and charitable endeavors, sports, and a variety of other kinds of programming – all with a local or regional focus.

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73 *See* Pick Declaration ¶ 11.

Comcast has been particularly successful in developing and distributing unique, high-quality, local and regional programming. The service now known as "cn8, The Comcast Network" was launched as The Comcast Network in September 1996. Combining the high production values of national cable programming with an emphasis on localized interests, The Comcast Network initially offered an exciting mix of locally focused call-in programs, regional sports coverage, and family entertainment. It quickly found an audience (receiving, for example, tens of thousands of attempted call-ins per month), and also enjoyed critical acclaim. As Comcast has grown, and built stronger clusters, cn8's reach, resources, and quality have all grown, too.

Today, cn8 is one of the nation's largest regional cable networks, serving 3.9 million homes in Pennsylvania, New Jersey, Delaware, and Maryland. It has become the region's most-honored 24-hour diversified network, with 31 Mid-Atlantic Emmy Award nominations in just four years. cn8 News, now two years old, offers two full hours nightly of news and discussions of regional issues, at 7 p.m. and at 10 p.m.[74] Customers have reacted positively, and overall ratings for cn8 increased over 100% during the past year. The success of this programming has enabled Comcast to expand the resources allotted to this endeavor.

Comcast also produces highly localized programming. In the Washington, D.C. area, for example, Comcast produces "Comcast Local Edition," five minutes of

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74 Last fall, cn8 offered the largest line-up of high-school football games in the nation, with at least one game every weekday afternoon. Press Release, cn8, *Comcast and CN8 to Offer Most Extensive High School Sports Coverage in the Nation* (Sept. 4, 2001), *available at*: <http://www.cn8.tv/press_release_display.asp?press_id=112> (71 games involving 103 high schools in Pennsylvania, New Jersey, and Delaware). And in October 2001, cn8 organized and transmitted a fundraising concert featuring Bruce Springsteen and Jon Bon Jovi to raise funds for Monmouth County (New Jersey) victims and survivors of the September 11 terrorist attacks.

programming every half hour (at 0:25 and 0:55) which appears on the channel carrying CNN Headline News.[75] These short programs include interviews with local government officials, discussions of local and regional issues, and promotion of charitable endeavors. The production and distribution of this programming can be highly localized; a Local Edition in Washington, D.C. may show an interview with a member of the D.C. City Council, while the system in Arlington, Virginia shows an interview with a member of that city's local school board. (Similar programming, with slight differences in emphasis, appears on other Comcast systems in Pennsylvania, New Jersey, Maryland, Delaware, Michigan, and Connecticut under the name "Comcast Newsmakers.")

These activities demonstrably benefit the communities in which Comcast operates. Comcast invests in programming like cn8 and Local Edition/Newsmakers as part of its commitment to public service. Such programming also strengthens the company's image in and connection to the communities it serves, offers potential customers a reason to sign up for Comcast's services, and offers existing customers one more reason to continue to subscribe.

The AT&T Comcast merger will make it possible to expand the areas in which these kinds of programs will be made available by extending Comcast's expertise and resources to areas in which AT&T Broadband has significant clusters. In addition, advertising revenue will increase to reflect the greater number of viewers, and this, too, will justify additional investment. These expectations are based, not on theoretical economic speculation, but on Comcast's own experience. For example, soon after Comcast acquired Greater Media's customers in Center City and South Philadelphia,

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[75] CNN Headline News makes these time slots available to other cable operators as well.

Comcast invested approximately $1 million to upgrade a newly acquired studio for cn8.[76] As the customer base grew, Comcast committed additional resources to the venture.[77]

In short, Comcast has the people, facilities, and experience to make local/regional programming work. Because these programs are designed as part of a "branding strategy," Comcast's local and regional programming skills and assets cannot feasibly be deployed to provide this kind of programming in areas where Comcast does not provide cable service. By contrast, they can and will be harnessed to extend quality local/regional programming to areas served by the merged AT&T Comcast.

D. The Merger Will Permit AT&T Comcast To Compete More Effectively In Selling National, Regional, And Local Advertising.

To date, cable operators have lacked the scale necessary to compete for national advertisers.[78] The merger, however, will create for the first time a cable company with the geographic reach to sell advertising on a national scale. In particular, the merged entity will have a market presence in 8 of the top 10 Designated Market Areas ("DMAs").[79] This will give AT&T Comcast a better chance to compete with

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76 Patricia Horn, *Cable Company Plans Upgrade of Philadelphia Studio*, Philadelphia Inquirer, July 28, 1999, 1999 WL 11407568.

77 Press Release, cn8, *CN8 to Expand New Jersey Television Coverage with the Opening of New News Bureaus* (Nov. 29, 2001), *available at*: <http://www.cn8.tv/press_release_display.asp?press_id=117> (new, fully-staffed, state-of-the-art news bureaus opened in Union and Toms River, New Jersey). cn8 currently has 20 studios (some are full-fledged production studios; others are lesser satellite facilities) in Pennsylvania, New Jersey, Delaware, and Maryland.

78 *See* Pick Declaration ¶ 29; *see also* Sallie Hofmeister, *Giant Cable Deal News Analysis: Merger Could Drive A New Round of Consolidation*, L.A. Times, Dec. 21, 2001, *available at:* <http://www.latimes.com/business/la-000100975dec21.story>.

79 Pick Declaration ¶ 29.

broadcasters, DBS, and other outlets in the sale of national advertising.[80] The total cable share of national broadcast advertising is and will remain small, but the merger will introduce a new alternative for national advertisers. At the same time, the potential increase in advertising revenues will help AT&T Comcast offset the costs involved in operating and improving its broadband service to consumers. The Applicants estimate that, even if the merged entity captures only 1% to 2% of the broadcast industry's current revenue for national advertising, it should be able to generate $100-200 million in increased EBITDA annually within one to three years after the merger by combining their national advertising sales efforts.[81]

In addition, the merger will create larger regional footprints,[82] permitting AT&T Comcast in some areas to compete more effectively in local and regional advertising markets. With a larger regional presence, the merged entity can offer advertising time throughout a region and a uniform channel placement selected by the advertiser. Instead of incurring the significant transaction costs of negotiating with many different cable systems in a region, a regional advertiser can take advantage of "one-stop shopping" in buying time on the cable systems serving the area it wants to target. In this way cable

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80 *See id.* ¶ 30. Broadcast television networks attract much larger audiences, and thus have generated much higher advertising revenues than cable. *See 2001 Video Competition Report* ¶ 78.

81 *See* Pick Declaration ¶ 31.

82 For example, AT&T Broadband and Comcast each operate cable system clusters in Connecticut and Pennsylvania; combining these systems will create a larger regional footprint in these areas.

systems can provide advertisers a more effective advertising outlet, although they will continue to have a small share of this market compared to broadcasters.[83]

E. The Public Interest Benefits Cannot Be Achieved Independently Of The Merger.

The efficiencies and synergies created by the merger – and the public interest benefits they will produce – cannot be obtained independently of a merger, such as through the formation of a joint venture. As Mr. Pick explains, there are a number of reasons for this conclusion.[84] In some cases, legal requirements may preclude joint ventures and collaborations among MSOs.[85] In other cases, the venture may involve such an unwieldy governance and ownership structure that efficient operation is effectively precluded.[86]

As the Commission has recognized, joint ventures also "raise[] complex problems at both the contract negotiation and implementation stages."[87] In a world of converging technologies and services, defining the joint venture service is very difficult. In contrast,

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83 *See* Diane Mermigas, *Bigger Piece of Pie Going to Comcast*, Electronic Media, Feb. 11, 2002, 2002 WL 9504681, at 3 (describing Comcast's current efforts to offer advertisers coverage throughout a DMA as a viable alternative to broadcasters). Cable operators in some instances enter into "interconnect" arrangements that allow them to compete more effectively with broadcasters in offering national and regional advertising. Under such an arrangement, an advertiser can run an advertisement on multiple cable systems throughout a region. Comcast, for example, has entered into interconnect arrangements with Time Warner and other cable companies in different regions of the country. Although these arrangements offer advertisers "one-stop shopping" in buying ad time on multiple cable systems serving a region, they can be difficult and time consuming to negotiate.

84 *See* Pick Declaration ¶¶ 32-33.

85 *See id.* ¶ 33.

86 *See id.*

87 *AT&T-MediaOne Merger Order* ¶ 175.

a merger "will create an alignment of the parties' economic interests that will reduce the areas of friction between the two companies and facilitate the development of telephony solutions."[88] The merger will permit full integration of the companies' operations, avoiding the transaction costs and uncertainties created by joint venture and other contractual relationships.

V. THE MERGER WILL NOT RESULT IN ANY VIOLATIONS OF THE COMMUNICATIONS ACT OR THE COMMISSION'S RULES.

The proposed merger will not result in the violation of any provisions of the Communications Act, other applicable statutes, or the Commission's rules. In particular, the proposed merger will not violate the reversed and remanded cable horizontal ownership limit, or any other multiple or cross-ownership limits, the foreign ownership limit, or any programming carriage or program access rules.[89]

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[88] *Id.*

[89] The Applicants have been, and will continue to be, in compliance with the relevant government restrictions on dealings between AOL Time Warner and AT&T. *See United States v. AT&T Corp. & MediaOne Group, Inc.*, No. CIV.A. 1:00CV01176, 2000 WL 1752108 (D.D.C. Sept. 27, 2000) (Final Judgment) (requiring AT&T to: (1) divest its interest in Road Runner on or before December 31, 2001; (2) restrict its role in the management and governance of Road Runner prior to divestiture; and (3) obtain prior approval of the Justice Department before entering into certain agreements with AOL Time Warner with regard to residential broadband service). AT&T has divested its interest in Road Runner, and has not entered into any agreements with AOL Time Warner that would require prior Justice Department approval. The Applicants also note that the Commission and the FTC imposed restrictions on AOL Time Warner as part of their respective merger reviews. *See AOL-Time Warner Merger Order* ¶ 272 (prohibiting AOL Time Warner from entering into certain agreements with AT&T); *America Online, Inc. & Time Warner Inc.*, Complaint, Docket No. C-3989 (Dec. 14, 2000), *available at*: <http://www.ftc.gov/os/2002/12/aolcomplaint.pdf> (FTC Consent Agreement) (prohibiting both exclusive and preferential agreements between AOL Time Warner and other cable operators). While these requirements were imposed on AOL Time Warner, not AT&T, AT&T has not entered into any agreements that would violate these prohibitions.

A. Cable Horizontal Ownership Limit

In October 1999, the Commission adopted a rule prohibiting a cable operator from having an attributable interest in cable systems that account for more than 30% of all MVPD subscribers nationwide.[90] In March 2001, the D.C. Circuit in *Time Warner II* reversed the 30% limit and remanded the rule to the Commission for further consideration.[91] In September 2001, the Commission adopted the *Horizontal Ownership FNPRM* to consider the cable horizontal issue in light of *Time Warner II*.[92] The Commission has not yet reached a decision in that proceeding.

AT&T Comcast will take all steps necessary to comply with any new cable horizontal ownership limit that may be adopted in connection with the pending *Horizontal Ownership FNPRM* proceeding. Moreover, using the dynamic market-power analysis required by *Time Warner II,* the Applicants demonstrate in section VI below that the merger will not have anticompetitive effects in any market or raise the types of buyer market power concerns that led Congress and the Commission to adopt a cable horizontal limit in the first place.

Moreover, the merger would not violate the 30% limit that was set aside in *Time Warner II*. AT&T Comcast will serve 29.87% of the nation's MVPD subscribers. This percentage is calculated as follows:

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90 *See Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992; Horizontal Ownership Limits*, 14 FCC Rcd 19098, ¶ 5 (1999) ("*1999 Horizontal Ownership Order*").

91 *See Time Warner II*, 240 F.3d at 1136; *see also Fox Television Stations, Inc. v. FCC*, Case No. 00-1222 (D.C. Cir. Feb. 19, 2002), *available at*: <http://www.fcc.gov/ogc/documents/opinions/2002/00-1222.html>.

92 *See generally Horizontal Ownership FNPRM.*

- AT&T Broadband has 13.44 million attributable subscribers in its owned and operated systems, 0.12 million attributable subscribers in its consolidated systems, and 5.24 million attributable subscribers in various partnerships (13.44 million + 0.12 million + 5.24 million = 18.80 million).[93]

- Comcast has 8.48 million attributable subscribers. This includes the 8.47 million subscribers served by Comcast's wholly-owned cable systems and the 0.01 million subscribers served by Clearview Partners in which Comcast holds an attributable interest (8.47 million + 0.01 million = 8.48 million).

- AT&T Comcast will therefore have 27.28 million attributable subscribers (18.80 million + 8.48 million = 27.28 million).

- There are 91.33 million total MVPD subscribers nationwide.[94] Thus, AT&T Comcast would be attributed with 29.87% of all MVPD subscribers (*i.e.*, 27.28 million divided by 91.33 million).

Because this percentage is below the horizontal limit in effect before the ruling in *Time Warner II*, there can be no reasonable basis for concern that the proposed merger would violate any horizontal ownership rule. Although the above calculation does not include the subscribers served by the TWE and TWI cable systems, as set forth in section V.F,

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[93] This total does not include Cablevision subscribers because, as noted above, AT&T Broadband's voting interest in Cablevision is now below 5% (and AT&T Broadband no longer has the right to appoint Board members to the Cablevision Board), and, therefore, Cablevision is no longer attributable to AT&T Broadband under the Commission's attribution rules.

[94] *See Kagan Media Money*, Jan. 29, 2002, at 9 (listing 91.33 million total MVPD subscribers); *see also 1999 Horizontal Ownership Order* ¶ 35 ("[I]n reviewing compliance with the rule, we will accept any published, current and widely cited industry estimate of MVPD subscribership."); *AT&T-MediaOne Merger Order* ¶ 17 n. 48 (relying on data provided by Paul Kagan Associates, Inc. in calculating total number of MVPD customers nationwide).

the Applicants intend to have no attributable interest in TWE at and after the closing of their merger.[95]

B. Cross-Ownership And Multiple Ownership Limits

AT&T Comcast will also be in full compliance with the Commission's various cross-ownership and multiple ownership rules.[96] Neither AT&T Broadband nor Comcast expects to own any attributable interest in a broadcast radio or television station, multichannel multipoint distribution service ("MMDS") system, or satellite master antenna television ("SMATV") system that would implicate the Commission's cable-broadcast cross-ownership or multiple broadcast ownership restrictions or the cable-MMDS or cable-SMATV cross-ownership restrictions.[97] Finally, neither company owns

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[95] If the TWE and TWI subscribers were counted, AT&T Comcast would serve approximately 38.63 million subscribers, or 42.30% of all MVPD subscribers. This is calculated as follows: (1) 18.80 million AT&T Broadband subscribers + 8.48 million Comcast subscribers + 11.35 million TWE/TWI subscribers (TWE and TWI actually serve approximately 12.8 million subscribers, but this includes 1.45 million subscribers served by the Time Warner-AT&T Broadband joint ventures in Texas and Kansas City that are already accounted for in the 18.48 million AT&T Broadband subscriber total) = 38.63 million subscribers; and (2) 38.63 million subscribers ÷ 91.33 million total MVPD subscribers = 42.30%.

[96] *See Fox Television Stations, Inc. v. FCC*, Case No. 00-1222 (D.C. Cir. Feb. 19, 2002), *available at*: <http://www.fcc.gov/ogc/documents/opinions/2002/00-1222.html> (vacating the Commission's cable/broadcast cross-ownership rule).

[97] *See* 47 C.F.R. § 73.3555 (broadcast multiple ownership limits); *id.* § 76.501(a) (cable/broadcast cross-ownership limit); *id.* § 21.912(a) (cable/MMDS cross-ownership limit); *id.* § 76.501(d) (cable/SMATV cross-ownership limit). AT&T Broadband owns 6 SMATV systems (see list attached as Appendix 10), but none of these owned entities will create a cross-ownership issue for the merged entity. Appendix 11 sets forth a list of Comcast SMATV systems. Comcast owns one SMATV system in the Hartford, Connecticut area where an AT&T Broadband owned and operated or consolidated cable system provides cable service. In addition, based on the available information, the Applicants are aware of one Comcast SMATV system in Lions Creek, Indiana, that is located in the franchise area of an AT&T Broadband non-consolidated cable system. Applicants envision that, promptly after closing, these SMATV systems will either be sold or integrated into the existing cable franchise (so that they are no longer operated

a financial interest greater than 10% or has any management interest in a LEC providing telephone exchange service within any of the other company's franchise areas. Thus, the merged entity will fully comply with the Commission's buyout restrictions.[98]

C. Program Access Rules

AT&T Comcast will be in compliance with the Commission's program access rules.[99]

D. Foreign Ownership Limit

AT&T Comcast will not have alien ownership that even approaches the benchmark of any applicable foreign ownership limit.[100]

E. Channel Occupancy Limit

Time Warner II reversed and remanded the Commission's channel occupancy rules,[101] and the Commission is now considering whether to retain the rules as part of its

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"separate and apart" from the franchised cable service in that area). *See* 47 U.S.C. § 533(a); 47 C.F.R. § 76.501(d). Finally, although Comcast owns a small number of SMATV systems in territories served by TWE cable systems, as discussed in section V.F, the Applicants intend to have no attributable interest in TWE at and after the closing of their merger.

98 *See id.* § 76.505(b) (LEC-cable buyout prohibition); *see also* 47 U.S.C. § 572(b) (statutory prohibition).

99 The Commission has rejected complaints filed by EchoStar Communications Corp. ("EchoStar") and DirecTV, Inc. ("DirecTV") that alleged Comcast violated the program access rules by refusing to sell terrestrially delivered regional sports programming to DBS competitors. *DirecTV, Inc. v. Comcast Corp and EchoStar Communications Corp. v. Comcast Corp.*, 15 FCC Rcd 22,802 (2000), *appeal pending sub nom. EchoStar Communications Corp. v. FCC*, No. 01-1032 (D.C. Cir. filed Jan. 19, 2001).

100 *See* 47 U.S.C. § 310(b) (limiting direct alien ownership interests in broadcast, common carrier, and aeronautical licensees to 20% and indirect alien ownership interests to 25%).

101 *See Time Warner II*, 240 F.3d at 1139.

remand proceeding.[102] AT&T Broadband and Comcast have nonetheless reviewed the channel lineups of all of their respective cable systems as of year end 2001. For purposes of these analyses, AT&T Broadband and Comcast counted all national video program services that are affiliated with AT&T Broadband and Comcast – and even Rainbow and TWE.[103] Based on these analyses, AT&T and Comcast have found that all of AT&T Broadband's cable systems and all of Comcast's cable systems will be in compliance with the remanded 40% channel occupancy limit post merger.

F. AT&T Broadband's TWE Interest

AT&T Broadband, through its wholly-owned subsidiaries, owns a limited partnership interest representing 25.51% of the senior priority (Series A) capital and residual equity capital of TWE.[104] Subsidiaries of AOL Time Warner hold the remaining

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[102] *See Horizontal Ownership FNPRM* ¶ 83 (inviting comment on whether "the Commission may relax, exempt specific cable operators from, or even forego imposing, vertical limits if the Commission determines that such a course of action would be justified given the prevailing market conditions").

[103] For the reasons discussed in sections II.B.2 and V.F, AT&T and Comcast do not believe it is necessary to count the TWE or Rainbow program services in their channel occupancy analyses. Even so, AT&T and Comcast have done so and found that, even counting these services, all of their systems will be in compliance with the remanded channel occupancy limit post-merger.

[104] Under a September 15, 1993 option agreement (originally entered into between TWE and U S WEST, MediaOne's predecessor in the TWE interest), AT&T Broadband obtained the right (when AT&T acquired MediaOne) to increase its Series A capital and residual capital interests in TWE, based on a sliding scale determined by the increase in TWE's average Cable Earnings Before Interest, Taxes, Depreciation, and Amortization ("Cable EBITDA") for the two prior calendar years over TWE's 1994 Cable EBITDA. AT&T Broadband may make a cash payment for this additional interest. Alternatively, AT&T Broadband may elect to exercise a cashless stock appreciation right in which the exercise price would be deducted from the increase in the partnership interest AT&T Broadband would otherwise receive, thereby resulting in a lower net increase amount. Prior to the end of 2001, AT&T Broadband commenced the process for exercising its option by requesting a determination of the fair market value of TWE. AT&T Broadband and TWE have retained an investment bank for the purpose of delivering that

74.49% limited partnership interests in the Series A capital and residual capital of TWE, as well as 100% of the junior priority (Series B) capital of TWE. TWE is a Delaware limited partnership that was formed in 1992 to own and operate substantially all of the business of Warner Bros., Inc., HBO, and the cable television businesses owned and operated by TWI prior to that time. AT&T Broadband acquired its interest in TWE in connection with the MediaOne acquisition. AT&T Broadband has appointed two directors to the TWE Board of Representatives ("TWE Board"). AT&T Broadband and Comcast are firmly committed to divesting AT&T Broadband's interest in TWE. The background of AT&T Broadband's interest in TWE as well as the Applicants' commitment to take the appropriate steps to divest and render this interest nonattributable are described below.

The *AT&T-MediaOne Merger Order.* In the *AT&T-MediaOne Merger Order*, the Commission determined that the merged AT&T-MediaOne entity would have an attributable interest in TWE's cable systems and programming services. As a result, the Commission found that the AT&T-MediaOne merger would violate the Commission's 30% horizontal subscriber limit, and required the merged entity to come into compliance with this limit by May 19, 2001.[105] After the D.C. Circuit in *Time Warner II* reversed

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determination. Following such delivery, AT&T Broadband will have 45 days in which to exercise its option. It is anticipated that any exercise of the option by AT&T Broadband will be a cashless exercise and will involve a net interest of less than 3%. The option represents value that AT&T Broadband is currently entitled to receive based upon TWE's past performance. If the option were not exercised at this time, AT&T Broadband would potentially lose this value under the terms of the option agreement.

[105] *See AT&T-MediaOne Merger Order* ¶¶ 18, 71 (specifying the three options for compliance, namely: (1) divest TWE, (2) terminate AT&T's involvement in TWE's programming activities (pursuant to the limited partnership exemption and the officers/directors attribution waiver provisions of the cable ownership attribution rules), or (3) divest other AT&T cable systems to bring AT&T below the 30% limit); *see also*

and remanded the 30% horizontal limit, the Commission suspended this compliance deadline "[i]n order to afford the Commission an opportunity to determine the relationship, if any, between the Court's decision on the ownership rules and the ownership conditions adopted in [the *AT&T-MediaOne Merger Order*]."[106]

In addition, as part of the AT&T-MediaOne merger, the Commission also imposed operational safeguards on the relationship between AT&T and TWE. The Commission intended these safeguards to serve as interim measures that would apply until AT&T came into compliance with the 30% horizontal subscriber limit. Although, as noted, the Commission has suspended this compliance deadline, it has determined that the safeguards would remain in effect.[107] The safeguards relating to TWE provide, among other things:

- An AT&T officer or director may not also serve as an officer or director of TWE. AT&T may, however, appoint as a TWE director an AT&T employee who is not an AT&T officer or director, as long as the employee is not involved in AT&T's video programming activities. AT&T officers, directors, and employees are prohibited from participating in any way in TWE's video programming activities;
- AT&T and TWE are prohibited from sharing information regarding the price, terms, and conditions for carriage of video programming; and
- AT&T is prohibited from obtaining a volume discount or other favorable terms and conditions from any video programming vendor as a result of TWE's purchase of video programming for, or carriage on, TWE's cable systems.[108]

Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from MediaOne Group, Inc., Transferor, To AT&T Corp. Transferee, 16 FCC Rcd 456 (2000) (determining that AT&T had elected to divest TWE to come into compliance with the 30% horizontal ownership limit).

106 *See AT&T-MediaOne Deadline Suspension Order,* 16 FCC Rcd 5835 (2001), *aff'd on reconsideration*, 16 FCC Rcd 20587 (2001).

107 *See AT&T-MediaOne Deadline Suspension Reconsideration Order*, 16 FCC Rcd 20587, ¶ 10 n.35 (2001).

108 *See AT&T-MediaOne Merger Order* at App. B, §§ 3-5 (safeguards relating to TWE).

Also, as part of the AT&T-MediaOne merger, the Commission adopted safeguards relating to AT&T's other programming interests, including Liberty Media, Cablevision/Rainbow, and certain video programmers owned in part by MediaOne that sell programming to TWE (*i.e.*, E! Entertainment, style., Food Network, Fox Sports New England, iN DEMAND, New England Cable News, The Outdoor Life Network, Speed Channel, and The Sunshine Network).[109] As noted, Liberty Media, Cablevision/Rainbow, Food Network, The Outdoor Life Network, Speed Channel, and The Sunshine Network are no longer attributable to AT&T. Accordingly, the only AT&T-MediaOne safeguards that continue to apply (in addition to the TWE safeguards described above) are those relating to E!, style., Fox Sports New England, iN DEMAND, and New England Cable News. These safeguards provide, among other things:

- AT&T is prohibited from attempting to influence, or otherwise participate in, the management or operation of these services.
- AT&T must instruct its representatives serving on the Boards or management committees of any of these services not to attend any Board or management committee meetings, or otherwise have contact with these program services. However, the safeguards do allow AT&T to file requests with the Commission to participate in matters not directly relating to video programming activities that would have a significant impact on any of these program services.[110]

The safeguards relating to TWE and AT&T Broadband's other programming interests also require AT&T to appoint a Corporate Compliance Officer and to engage an independent auditor to conduct an examination every six months of AT&T Broadband's compliance activities. In addition, penalties are prescribed for AT&T's failure to comply

[109] Although MusicChoice was included in this list, it should not have been, as it is a digital *audio* service, not a video programming service.

[110] *See AT&T-MediaOne Merger Order* at App. B, §§ 12-15 (safeguards relating to MediaOne video programming interests).

with the safeguards or reporting requirements. AT&T has appointed a Corporate Compliance Officer and engaged PricewaterhouseCoopersLLP as the independent auditor. AT&T has filed three compliance reports with the Commission since the closing of the AT&T-MediaOne merger. These reports provide details regarding the specific steps AT&T has taken and continues to take to comply with the safeguards.[111]

AT&T Broadband Has No Role In Or Ability To Influence The Management Of TWE. Under the TWE Limited Partnership Agreement ("LPA"),[112] AT&T Broadband has no role in or ability to influence the management or operations of TWE, including its video programming-related activities. AT&T Broadband does not have the right under the LPA to communicate with TWE, or AOL Time Warner, the general partner of TWE, on matters pertaining to the day-to-day operations of TWE or its video programming interests. Under the terms of the LPA, the TWE Cable Management Committee (all members of which are appointed by and from AOL Time Warner) has full discretion and final authority over TWE's cable operations. All of MediaOne's rights with regard to the TWE Cable Management Committee were terminated *before* AT&T merged with MediaOne and acquired the TWE interest.[113] The TWE Cable Management

[111] These reports were filed in CS Docket No. 99-251 on December 15, 2000, June 15, 2001, and December 17, 2001.

[112] The Applicants will submit this document upon adoption of a protective order in this proceeding.

[113] *See* AT&T *Ex Parte* Comments, CS Docket No. 99-251, at 9-10 (filed Nov. 24, 1999); AT&T *Ex Parte* Reply Comments, CS Docket No. 99-251, at 5-6 (filed Dec. 21, 1999). The TWE LPA contains a non-compete clause that precluded MediaOne from engaging in certain lines of business in competition with Time Warner. *See* TWE LPA § 5.5(a). However, MediaOne had the right unilaterally to eliminate the non-compete clause, *see id.* § 5.5(f), and on August 3, 1999, it did so. When the non-compete was eliminated, the TWE LPA then gave Time Warner the right to remove MediaOne's TWE management rights. *See id.* On August 4, 1999, Time Warner sent notice to MediaOne

Committee's decisions are binding on the TWE Board. The TWE Board has never met, and the extent of the Board's power (should it ever meet) and of AT&T Broadband's involvement on that Board is strictly limited to certain extraordinary "investor-protection" matters should any arise – such as the merger of TWE, the sale of more than 10% of TWE's assets, or TWE's voluntary bankruptcy – and not to any operational matter.

Planned Divestiture Of AT&T Broadband's Interest In TWE. AT&T Broadband and Comcast do not view the TWE interest as a long-term investment and are firmly committed to divesting the interest for a reasonable price as quickly and efficiently as possible.[114] The process of attempting to sell the interest is already underway. AT&T Broadband has pursued with AOL Time Warner various options for the sale of its TWE interest to AOL Time Warner in an efficient and expeditious manner. AT&T Broadband also is pursuing its option to sell its TWE interest via a public offering pursuant to a contractual right to registration rights.

AT&T Broadband has taken a number of steps to advance the registration rights option for the sale to the public of the TWE interest. That process began in February

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that it was immediately terminating all of MediaOne's management rights with regard to TWE that it was entitled to terminate, including *all rights* with regard to the Cable Management Committee. (The Applicants will submit this document upon adoption of a protective order in this proceeding.) *See also* Time Warner Entertainment Company, L.P., SEC Form 8-K, at 2 (Aug. 5, 1999) (noting that "MediaOne no longer has a vote on or any right to participate in the Cable Management Committee") (copy attached as Appendix 12). This occurred prior to the merger of AT&T and MediaOne. Thus, when the merger was closed, AT&T did not acquire any ability to participate in the management or operation of TWE, nor has it attempted or had the right to participate in the management or operation of TWE since the merger.

[114] The Applicants, in fact, have a strong business incentive to divest AT&T Broadband's interest in TWE to further improve the merged entity's ability to finance capital expenditures. *See supra* section IV.A.

2001 when AT&T submitted a request to TWE, pursuant to the TWE LPA, that TWE reconstitute itself as a corporation and register for sale in an initial public offering an amount of equity securities (representing converted partnership interests) held by AT&T Broadband (up to the full amount held by AT&T Broadband) determined by an independent investment banking firm so as to provide sufficient trading liquidity and minimize any initial public offering discount. Once AT&T Broadband exercised its registration rights, AT&T Broadband and AOL Time Warner each were required to select investment banking firms which then would jointly select a third investment banking firm to value the partnership. AT&T Broadband named Credit Suisse First Boston as its investment banker for the registration process and AOL Time Warner has named Bear Stearns as its investment banker.

Although the registration rights process has not proceeded as smoothly as AT&T would prefer, and AT&T does not have the ability unilaterally to compel AOL Time Warner's timely cooperation in the process, the registration rights process is now being actively pursued. For example, recently, AT&T Broadband and AOL Time Warner agreed in principle that Banc of America Securities LLC would be the third investment banker to perform the critical function of establishing a value for TWE as part of the registration process. The parties are in the process of negotiating the terms of the Banc of America Securities LLC engagement letter.

The next steps involve, among other things, the third investment banker determining the "registrable amount" and "appraised value" of the converted securities. The registrable amount is the maximum amount of converted securities that can be registered and sold in the IPO without suffering an unreasonable IPO discount. The appraised value is the price at which the registrable amount of converted securities could be sold in a public offering after deducting underwriters' discounts and commissions. Both the registrable amount and the appraised value are highly dependent on current market conditions.

Once the registrable amount and the appraised value are established, TWE may elect either to reconstitute itself as a corporation and register securities equal to the registrable amount or not to reconstitute itself. If TWE elects not to reconstitute itself, AT&T Broadband will have certain "put" rights to require TWE to purchase a portion of AT&T Broadband's partnership interests equal to the registrable amount at a price equal to the appraised value and, if AT&T Broadband exercises that right, TWE will have a "call" right to purchase the remainder of AT&T Broadband's partnership interest. If TWE elects to reconstitute itself, it must promptly commence the process of converting itself into a corporation and registering the securities for sale in a public offering. If TWE elects to pursue a public offering and the aggregate price for which the securities are to be offered to the public (as determined by the managing underwriter for the offering) is less than 92.5% of the appraised value, then TWE has the right to cancel the offering and purchase either all or the offered portion of AT&T Broadband's interest.

The registration rights process is complex and difficult. Further, because it is affected not only by TWE and AOL Time Warner's actions, but also by prevailing market conditions, the process is not subject to unilateral control by AT&T Broadband. Nonetheless, AT&T Broadband is firmly committed to take all the steps necessary to achieve the sale of the TWE interest through the registration rights process and to do so as expeditiously as possible. In addition, as a result of the deemed transfer that may occur as a result of this transaction, the TWE partnership agreement may require that AT&T Broadband give AOL Time Warner a "right of first refusal" to purchase AT&T Broadband's interest in TWE in advance of closing of the merger. If AT&T Broadband offers AOL Time Warner this right of first refusal, AOL Time Warner would have the option to buy the interest. Although AT&T Broadband remains confident that its contractual rights under the partnership agreement will allow it to divest satisfactorily the TWE interest via registration rights, AT&T Broadband will pursue all its options. As can be seen, AT&T Broadband's ultimate ability to dispose of its interest lies in the hands of AOL Time Warner and the public markets, neither of which it can control.

Elimination of Any Attributable TWE Interest By The Time Of Closing. The Applicants intend to have no attributable interest in TWE at and after closing. As noted, AT&T Broadband and Comcast are firmly committed to divesting the TWE interest. The Applicants describe above the actions that have recently been taken to accomplish that result and the basis for their belief that they will be able to divest TWE in a manner that is entirely satisfactory to the Commission. In the event that the sale of the TWE interest to a third party or parties has not been completed when the Applicants are ready to close the merger, AT&T, if it has not already done so, is prepared to take the steps that may be necessary to insulate the interest under the Commission's rules before it transfers that interest to AT&T Comcast. In addition, Comcast and AT&T Broadband will take such additional steps, if any, as may be appropriate to ensure that AT&T Comcast would not be able to influence TWE prior to its ultimate sale.

Since the time that the Commission considered the question of whether AT&T's interest in TWE could be insulated and determined that it could not, the court in *Time*

Warner II vacated the "program sale" aspect of the Commission's attribution rules. That decision allows AT&T to insulate its interest in TWE, pending divestiture, in a straightforward manner. The Commission's rules allow a limited partner to demonstrate that it is not materially involved in the management or operation of the video programming-related activities of a limited partnership, and that its partnership interest is therefore nonattributable for purposes of the cable horizontal ownership limit. In particular, the limited partner may: 1) certify that it has complied with the Commission's seven insulation criteria,[115] and 2) obtain a waiver for any representatives on the partnership's Board, so long as those representatives are recused from the video programming-related activities of both the partnership and the limited partner.[116]

In the Applicants' view, AT&T Broadband satisfies the seven insulation criteria because it: (1) is not an employee of the TWE partnership; (2) is not an independent contractor or agent of the TWE partnership; (3) does not communicate with TWE, or AOL Time Warner, the general partner of TWE, on matters pertaining to the day-to-day operations of TWE's video programming business; (4) is subject to a veto by TWE's general partner with regard to any vote on the admission of new general partners to TWE;[117] (5) has no rights to remove TWE general partners; (6) does not perform any

[115] *See Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992; Horizontal Ownership Limits*, 14 FCC Rcd 19014, ¶ 57 n.163 (1999).

[116] *See* 47 C.F.R. § 76.503 (note 2(c)).

[117] *See* TWE LPA § 12.1(c)(i)(G). The admission of a new general partner requires the consent of *both* AOL Time Warner's and AT&T Broadband's representatives on the TWE Board of Representatives. Consequently, AOL Time Warner may exercise veto power over the admission of any new general partner by simply refusing to approve such admission.